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SIPDIS
SENSITIVE

DEPARTMENT FOR EEB/IFD/OMA - JWINKLER AND EEB/CBA - DWINSTEAD

DEPT OF TREASURY WASHDC FOR ANDY BAUKOL, DANIEL PETERS, REBECCA KLEIN

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SUMMARY

¶1. (SBU) In a March 12 visit to Ethiopia, Acting Assistant Secretary of Treasury, Andy Baukol, found a Government of Ethiopia (GoE) that has become more vocal about its need for sustained aid flows from the West and more recalcitrant about implementing any reforms or liberalization of key sectors such as banking and telecommunications. Baukol noted that without reforms and adjustment, Ethiopia was unlikely to resolve a balance of payments crisis of its own making and could likely face a deeper and longer recession than the broad global recession. GoE interlocutors responded defensively by arguing that the World Bank (Bank) and International Monetary Fund (IMF) do not know the right economic policies and should just provide faster, unconditioned aid to bolster Ethiopia's proven record of strong growth. Despite the rhetoric, the GoE meetings made clear that the GoE has not developed any sort of domestic plan or fiscal solution, besides reliance on external aid, to offset the effects of the global financial crisis. END SUMMARY.

ECONOMIC SLUMP IS WEST'S FAULT SAYS GOE

¶2. (SBU) In response to Baukol's inquiry into the effects of the global crisis on the Ethiopian economy, Minister-ranked Chief Economic Advisor to the Prime Minister Newaye Gebre-ab argued that Ethiopia's closed banking system somewhat insulated the country from the banking debacle around the world. Still, Newaye conceded that Ethiopia has already started to feel the "second order" effects of the global crisis, as heavy declines in coffee exports have been registered. The Treasury officials emphasized reform, particularly in banking and telecommunications, as a potential avenue for Ethiopia to offset the impact of the global recession on its exposed export sectors. Despite this advice, Newaye made clear that

Ethiopia was committed to maintaining its status quo economic principles (particularly regarding the closed banking and telecommunications sectors), largely discounting the reform message. Newaye argued that the West's key role in precipitating the economic turmoil would unfairly penalize Ethiopia and other African countries that remain innocent bystanders in the current crisis, and suggested, therefore, that the West has an obligation to provide relief. Newaye explained that Africa would have to bear an asymmetrical burden as "second order" effects of the crisis eventually collapse trade in commodities and jeopardize aid to Africa. Newaye lamented that Ethiopia and Africa's unfavorable economic circumstances resulted from flawed Western economic principles and excesses which ultimately led to the crisis.

AID NOW, NOT LATER

¶3. (SBU) Although Newaye blamed the West for Africa's current economic problems, he remained fervently committed to Ethiopia's position that aid should be sustained to Africa amid the economic crisis. Aid is key over the short- and medium-term for Ethiopia to emerge unscathed from the current global recession. He contended that the money Ethiopia and Africa needed to survive the downturn would be a trifle compared to the recent rounds of stimuli and bailouts seen in the U.S. and Europe. He suggested that the marginal returns that the many rounds of stimuli had provided in the West would have generated significantly higher returns in Africa for a fraction of the cost. Newaye openly asked the Treasury officials what it would take for Ethiopia to achieve a minimum level of support from the West to maintain aid and prop up trade. He contended that the West needed to scale down its reform-oriented rhetoric and, moreover, treat Ethiopia and Africa with a bit more modesty and fairness during the crisis, particularly since they

(Africans) are not to blame for the current crisis.

ETHIOPIA'S PERFORMANCE ALONE WARRANTS AID

¶4. (SBU) The overriding consensus from GoE interlocutors was that Ethiopia's stellar economic performance over the last 15 years warrants increased support through quickly-disbursed, unconditioned aid. Newaye explicitly argued that the World Bank and IMF "do not know what the right economic policies are." He explained that the quick disbursement of aid would be the stimulus that would keep Ethiopia's economy growing at the government professed levels of 11 percent during the global downturn. (Note: Although the GoE is adamant in perpetuating the myth of sustained 11 percent annual growth for the past five years, the assessments shared by us, the IMF and World Bank internally, is that growth has been closer to seven to eight percent. End Note.) Moreover, the Minister explained that Ethiopia has come close to meeting many of its development goals. He argued that this resulted from the GoE's strong economic policies and that much of these gains would have been undermined if Ethiopia had adopted policy recommendations from the Bank or IMF earlier. In a separate meeting with the Treasury delegation, State Minister for Finance Mekonnen Manyazewal also echoed Ethiopia's previous stellar economic performance as a real benchmark for progress and achievement of development goals.

¶5. (SBU) Minister Newaye said that "although the GoE remains sensitive to the USG's comments and advice on reform, it requests that the USG suspend judgment about Ethiopia's perceived policy or economic shortfalls and focus merely on its real progress over the long term." Newaye explained that the GoE is open to real policy reforms in the future in order to stabilize and grow its economy. The Minister did not elucidate the type or manner of reforms when queried by the Treasury officials. However, he did say that any reforms would need to follow a workable timeline and the government would need enabling institutions in order to support policy shifts. Interestingly, the Minister's main argument of increased aid, without conditions, was buttressed by his claim that Ethiopia is looking to limit its reliance on India and China for soft loans.

The Minister contended that the GoE would rather avail itself of the IMF and World Bank facilities than rely solely on the Chinese and Indians for external financing.

PRIVATE SECTOR AND DONOR RESPONSE MIXED

¶6. (SBU) Over lunch with private sector representatives, participants argued that Ethiopia still remains attractive for investment opportunities. However, the private sector has become increasingly concerned about the acute foreign exchange crisis and the perception of Washington's diminishing role and participation in Ethiopia and Africa's economic development. One individual referenced the recent announcement by China to establish a USD 5 billion sovereign fund for Africa's development. They asked why Washington was not looking at establishing a program similar to the Chinese fund. Although, the private sector officials at the lunch recognized that the foreign currency crisis was choking the domestic economy, some privately intimated that it was a good wakeup call for the GoE.

¶7. (SBU) In contrast, Ambassadors from major donor nations painted a picture of an Ethiopian economy in more dire straits. Pointing to sustained negative real interest rates, the second-highest rate of inflation in Africa, and foreign exchange reserves capable of covering only four weeks of imports, the assembled diplomats stressed the need for the GoE to release its tight control of the economy. In particular, donor Ambassadors noted the need to create a conducive environment for investment beyond Ethiopia's traditional sectors and to liberalize the foreign exchange regime to avoid the perpetuation of the current crisis. Participants showed consensus in their views that the closed financial services and telecommunications sectors detract particularly from Ethiopia's ability to attract foreign investment and the dominance of state- and party- owned enterprises in the economy further stymie the development of a robust private sector.

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COMMENT

¶8. (SBU) The GoE's resistance to medium or long-term economic reforms or benchmarks in order to offset negative impacts of the global financial crisis only makes worse an already dire economic situation in Ethiopia as inflation remains significantly double digit and the government reels from a severe balance of payments crisis. Additionally, with the recent production halt of Coca Cola in Ethiopia (Ref A) as a result of the country's forex crisis (Ref B), it is not clear if the GoE understands the severity of the global financial crisis' deleterious effects on foreign direct investment and economic growth prospects in Ethiopia.

¶9. (SBU) Despite Ethiopia's clear challenges, the GoE is lauding the recent pledges by the G-20 to increase the IMF's lending capacity and flexible financing regime without conditions or requiring real reforms as a victory. Public statements suggest that the GoE sees the G-20's pledges as a validation of their previous economic policies, where absolute performance, not long-term reform, reigns. Some GoE officials believe that Ethiopia is poised to receive USD 400 million from the IMF and significantly increased assistance from the Bank without adopting macroeconomic reforms. We know that economic growth and performance figures have been grossly inflated by the GoE, the country's macroeconomic imbalances are endogenous, and the GoE does not have a clear strategy to correct them. As such, although the IMF's increased lending capacity and flexible financing programs will spur growth in the short-term in Ethiopia, we believe that more, faster, and unconditioned aid to Ethiopia will only serve as a band-aid, deferring the much needed macroeconomic adjustments to another day. To advance the U.S. objective of promoting sustainable economic prosperity, our bilateral assistance, and our votes on assistance from multilateral sources, should continue to be linked to, and contingent upon, economic policy reforms and performance indicators. END COMMENT.